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July 22, 2011

Jennifer J. Johnson
Secretary, Board of Governors of the
Federal Reserve System
20th Street and Constitution Avenue, NW.
Washington, DC 20551

Re: Docket No. R-1417 (Regulation Z; "Ability to Repay")

Dear Ms. Johnson:

The California Bankers Association appreciates this opportunity to submit these comments to the Federal Reserve Board in response to its proposed rule to implement the ability-to-repay requirements for closed-end residential loans as mandated by the Dodd-Frank Wall Street Reform and Consumer Financial Protection Act of 2010 (the "Act"). CBA is a professional nonprofit organization established in 1891 and represents most of the FDIC-insured depository financial institutions doing business in the state of California. We understand that the completion of this proposed rule may also involve the Bureau of Consumer Financial Protection; therefore, we address these comments to both agencies.

General Comments

CBA's members support the observance of prudent underwriting standards and procedures that, among other things, ensure that prospective borrowers are likely to be able to repay their loans. We recognize that the Board is required by the Act to issue rules on specific procedures. However, we call upon the Board to exercise its discretion as a major bank regulator to avoid in the final rule the imposition of inflexible data and documentation requirements. Record retention and the need to establish audit trails to demonstrate compliance (such as by obtaining IRS transcripts to verify a borrower's income) would tax banks' resources and make them aversive to making loans. If the Board's rule will create burdensome and useless paper documentation, this would only serve to make loans more expensive and thus reduce the availability of residential loans to low and moderate income borrowers as well as some quality buyers.

Moreover, to burden the industry with meticulous rules would almost certainly expose lenders to liability from enterprising trial attorneys based on technical violations.

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All this means that the housing market will continue to suffer, and without a recovery in housing the economy will also be slow to recover. We urge that the Board take steps to strike a balance between consumer protection and facilitating the availability of consumer credit.

Safe Harbor

The Act provides for a safe harbor from liability if a loan is underwritten pursuant to the qualified mortgage standards. CBA supports the Board's Alternative 1, which would treat qualified mortgages as enjoying a legal safe harbor as opposed to providing merely a rebuttable presumption of compliance. In light of the significant expansion of penalties and liabilities associated with not meeting these criteria, the availability of a sound legal safe harbor is vital for the preservation of a viable mortgage market. It would also go far to give investors of qualified mortgages greater confidence that their investments would not be subject to future liability based on judicial interpretations that would jeopardize a "safe harbor" based on a rebuttable presumption of compliance. The Board should specifically clarify that a qualified mortgage is not subject to a private right of action.

Points and Fees

Compensation paid directly or indirectly by a consumer or creditor to an employee of a loan originator should not be counted in the points and fees test. For example, including compensation (such as incentive payments) paid by a bank to its own employee loan originator would severely tax a bank's ability to meet the criteria for qualified mortgages. This proposal simply ignores the realities of how creditors need to structure their compensation to their mortgage professionals in a manner that makes business sense to the creditor and their employees. Also, the Board is of course mindful of the close connection in this regard to the mortgage loan originator compensation rule. Banks will need greater clarity with respect to originator compensation.

CBA agrees with the proposed exclusion for bona fide third party charges that are not retained by the creditor from the definition of "points and fees." Some of these arrangements, such as the payment of private mortgage insurance (PMI), result in a lower monthly payments by borrowers, and not excluding them would not benefit borrowers.

Prepayment Penalties

We oppose the provision in the Proposal that would include within the definition of prepayment penalty closing costs that are waived but that can be recouped in the event of prepayment. This is an unwarranted extension of the traditional understanding of the term.

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Verification of Third-Party Records

CBA supports the proposed official staff commentary clarifying that a creditor's own records can be treated as "third-party records" for purposes of verification. This is a common sense rule that benefits both creditors and borrowers. We also support permitting consumers to orally verify their military employment status as proposed. And we agree that creditors should not be required to verify debts that a consumer lists on an application that do not appear on the consumer's credit report.

Balloon-Payment Qualified Mortgage in Rural Areas

The Act includes a provision creating an exception to the definition of qualified mortgage for a balloon payment loan that meets certain criteria, including that the creditor operates in a predominately rural area. We ask that the Board exercise its broad discretion where appropriate to broaden this exception, and not rely on simple, numerical tests intended to apply nationally. The concept of what is "rural" in the vibrant Central Valley of California may well differ markedly from what is considered rural in the plains of Kansas. An overly restrictive set of criteria would unnecessarily exclude too many loans that meet the intent of the exception. We would also support raising the total annual residential mortgage originations a creditor may make in order to qualify for the balloon-payment qualified mortgage exception to at least 1000 loans.

Conclusion

CBA appreciates this opportunity to provide comments. We acknowledge that Congress through the Dodd-Frank Act set forth what could be construed as specific and prescriptive operational standards for mortgage lenders. We believe that the Federal Reserve Board and the Bureau of Consumer Financial Protection have ample discretion to implement the provisions in the Act in a manner that preserves the all-important ability of mortgage lenders to conduct their business effectively, and without having to labor under unnecessary burdens and risks of legal liability. Congress did not intend by the Act to make mortgage loans unnecessarily expensive and thus less available to credit-worthy consumers. For these reasons, we ask that CBA's comments, as expressed above, be seriously considered. Thank you for your attention.

Sincerely,



Leland Chan
General Counsel